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November 8, 1999

**BY HAND DELIVERY**

Ms. Magalie Roman Salas  
Secretary  
Federal Communications Commission  
445 12<sup>th</sup> Street, S.W.  
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION  
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**Re: BT North America Inc. Petition for Reconsideration  
In the Matter of Direct Access to the INTELSAT System,  
Report and Order, IB Docket No.: 98-192 (released Sept. 16, 1999)**

Dear Ms. Salas,

BT North America Inc., pursuant to Section 1.429 of the Commission's Rules, 47 C.F.R. §1.429, hereby files an original and eleven copies of its Petition for Reconsideration of the Commission's Report and Order in the above-captioned proceeding.

Please direct questions concerning this Petition to the undersigned at (202) 434-8882.

Respectfully submitted,

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**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

**In the Matter of**

**Direct Access to the  
INTELSAT System**

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**IB Docket No. 98-192  
File No. 60-SAT-ISP-97**

**RECEIVED**  
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FEDERAL COMMUNICATIONS COMMISSION  
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**BT NORTH AMERICA INC. PETITION FOR RECONSIDERATION**

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**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

<b>In the Matter of</b>	)	<b>IB Docket No. 98-192</b>
	)	<b>File No. 60-SAT-ISP-97</b>
<b>Direct Access to the</b>	)	
<b>INTELSAT System</b>	)	

**BT NORTH AMERICA INC. PETITION FOR RECONSIDERATION**

BT North America Inc. ("BTNA") hereby petitions for reconsideration of the Commission's Report and Order in the above-captioned proceeding,<sup>1</sup> pursuant to Section 1.429 of the Commission's Rules, 47 C.F.R. § 1.429.<sup>2</sup> BTNA demonstrates in this petition that the Commission must eliminate the surprise restriction that it placed on foreign Signatories and their greater than fifty percent owned affiliates (collectively "foreign Signatories") in the *Direct Access Order*, denying them direct access to INTELSAT for service between the U.S. and any foreign country in which the Signatory uses 50 percent or more of all INTELSAT capacity consumed in that country.<sup>3</sup>

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<sup>1</sup> *In the Matter of Direct Access to the INTELSAT System*, IB Docket No. 98-192, File No. 60-SAT-ISP-97, FCC 99-236 (released Sept. 16, 1999) (hereafter "*Direct Access Order*" or "*Order*").

<sup>2</sup> BTNA is a subsidiary of British Telecommunication plc, the INTELSAT Signatory in the United Kingdom. The United Kingdom has permitted Level 4 direct access to INTELSAT since 1994. BTNA is directly affected by this surprise prohibition because it operates a growing satellite business in the U.S. on the U.S./U.K. route and would be prevented under the rule from purchasing INTELSAT satellite service on that route at the lower direct access rates that its competitors will pay.

<sup>3</sup> *Id.* at ¶98.

## I. INTRODUCTION AND SUMMARY

In its *Direct Access Order*, the FCC takes a step toward reducing the cost to consumers of international satellite service through INTELSAT. By permitting retail carriers and companies other than Comsat to purchase satellite capacity directly from INTELSAT at the INTELSAT utilization charge (“IUC”) rates available to Signatories,<sup>4</sup> consumers will avoid the needless cost burden of paying high mark-ups to Comsat, which has been both the mandatory and exclusive wholesaler of such capacity. The new direct access regime will also improve competition in the field by placing Comsat and other retailers on a more equal footing. <sup>5</sup> With this new course of action, the U.S. finally joins the 100 other countries that permit direct access. <sup>6</sup>

Regrettably, the FCC undercut the value of this important policy with its stunning decision to limit direct access to a class of potential competitors, the foreign Signatories. This restriction, which was adopted without benefit of public notice and comment, is anti-competitive and serves no beneficial public purpose. Indeed, the Commission's explanation for the restriction defies reasoned analysis and fundamental economic principles. The Commission would best serve the public interest by eliminating this unnecessary and harmful rule that denies U.S. consumers the full benefits of competition.

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<sup>4</sup> In addition to the duration of lease, factors used to determine an IUC include bandwidth and power used. IUCs are listed in the INTELSAT tariff manual. *See Id.* at ¶7.

<sup>5</sup> As BTNA demonstrated in its Comments in this proceeding, a direct access environment would be even more competitive and fully sustainable for Comsat if, as in the U.K., U.S. carriers and users were not charged for Signatory-related expenses such as the 5.58% Signatory surcharge fee suggested in the *Order*. *Id.* at ¶¶87-93.

<sup>6</sup> INTELSAT, September 24, 1999. The most recent tabulation by INTELSAT shows 65 countries permitting Level 3 direct access and 35 countries permitting Level 4 direct access. Of the 65 countries allowing Level 3, 19 are non-member country D.A.T.E.s (“Duly Authorized telecommunications Entities”).

## II. THE FCC FAILED TO PROVIDE THE NOTICE AND OPPORTUNITY FOR COMMENT THAT THE LAW REQUIRES

The Commission adopted the foreign Signatory prohibition without notice and opportunity for public comment, in violation of Section 553 of the Administrative Procedure Act ("APA"). <sup>7</sup> The APA requirement reflects fundamental considerations of fairness and opportunity to be heard. The notice and comment procedure also provides the means for the FCC to test its proposed policies and the factual determinations that underlie its decision-making against the weight of informed public comment. In this proceeding the FCC denied the public a fair hearing as to whether a foreign Signatory restriction is in the public interest, and the Commission denied itself the opportunity to receive informed comment on that important matter. The result was the adoption of a rule that is flawed in both theory and substance.

Contrary to the requirements of the APA, in this case "parties affected by a final rule were [never] put on notice that 'their interests were at stake.'" <sup>8</sup> The Notice in this proceeding simply contains no proposal to restrict foreign Signatories from participating in direct access. Nor is the restriction a "logical outgrowth" of proposals contained in the Notice. <sup>9</sup> This Petition is the first opportunity for BTNA and other parties with interests at stake to offer comments on this rule and its underlying theory.

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<sup>7</sup> 5 U.S.C. § 553(c).

<sup>8</sup> *American Medical Assoc. v. U.S.*, 887 F.2d 760, 768 (7<sup>th</sup> Cir. 1989) (citing *Spartan Radiocasting Co. v. FCC*, 619 F.2d 314, 321 (4<sup>th</sup> Cir. 1980).

<sup>9</sup> *American Water Works Assc. V. EPA*, 40 F. 3d 1266, 1274 (D.C. Cir. 1994); *Public Service Commission of the District of Columbia v. FCC*, 906 F. 2d 713, 717 (D.C. Cir. 1990). Whether the final rule is a "logical outgrowth" or whether another round of comment is required is a functional standard, that is, would "a new round of notice and comment . . . provide the first opportunity for interested parties to offer comments that

The *Notice* neither states nor implies that the FCC was considering restrictions on foreign Signatories.<sup>10</sup> In the section of the *Notice* concerning alleged competitive concerns raised by direct access, the Commission seeks comment on several issues related to INTELSAT's immunity from regulatory jurisdiction,<sup>11</sup> and seeks comment on concerns if the FCC permits direct access to U.S. carriers with significant ownership in undersea cable facilities.<sup>12</sup> At no point in this section, or elsewhere in the *Notice*, does the Commission suggest that parties should address whether there are competitive concerns if a foreign Signatory seeks direct access as a U.S. carrier.<sup>13</sup>

Nor is the rule a "logical outgrowth" of party comments submitted in response to the *Notice*. Only Comsat submitted comments discussing a theory of competitive harm, but even Comsat's comments present a starkly different harm and remedy than that established in the *Order*. The theory advanced by Comsat suggested risks not posed by foreign Signatories acting as U.S. direct access users but rather, risks posed by large U.S. carriers who may influence foreign Signatories acting as bilateral correspondents and co-

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could persuade the agency to modify its rule." *American Water Works Assc.*, 40 F.3d at 1274.

<sup>10</sup> *In the Matter of Direct Access to the INTELSAT System*, IB Docket No. 98-192, File No. 60-SAT-ISP-97 at ¶56 ("NPRM" or "Notice").

<sup>11</sup> *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> In the absence of such specific notice, the Commission's open-ended request for comment on "what other regulatory protection might have to be imposed?" *id.* at ¶57, likewise must fail to constitute sufficient general notice that foreign Signatories were expected to justify why they should not be separated out for disparate treatment in a final rule. *See, e.g., American Iron and Steel Institute v. EPA*, 568 F.2d 284, 293, (3<sup>rd</sup> Cir. 1977) (agency's notice must "fairly apprise interested persons of the 'subjects and issues' [of the rule making]."). The word "Signatory" does not even appear in the relevant Section of the *NPRM*, at ¶¶56-58.

owners of cable systems.<sup>14</sup> This theory suggests that foreign Signatories may be coerced, and indirectly led, by a “powerful coalition” of large U.S. carriers who will “compensate” the Signatories to manipulate IUC rates to the advantage of the U.S. carriers. Comsat’s remedy for this and other alleged competitive risks would be to bar direct access to all parties.<sup>15</sup> However, it is clear that Comsat’s immediate concern is with the incentives and abilities of large U.S. international carriers. Yet the Commission creates a new theory that is completely different from Comsat’s comments, implicitly dismissing concerns with the incentives of large U.S. carriers and focusing for the first time on the possible incentives of foreign Signatories.<sup>16</sup>

In sum, the FCC deprived the public in violation of law of an essential element of reasoned decision-making by issuing the foreign Signatory restriction without providing interested parties adequate notice and opportunity to be heard. As shown below, the restriction adopted by the Commission is not supported by reasoned analysis, its purported rationale is contrary to fundamental economic principles and its effect is anti-competitive and anti-consumer.

### **III. THE FOREIGN SIGNATORY RESTRICTION IS NOT SUPPORTED BY REASONED ANALYSIS**

The reasoning underlying the foreign Signatory restriction adopted in this proceeding is fundamentally flawed. BTNA demonstrates below that no foreign

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<sup>14</sup> See Comments of Comsat Corporation at 66-67 (citing Statements of Professors Jerry R. Green and Hendrick S. Houthakker, Harvard University, and Johannes P. Pfeifenberger, The Brattle Group, *An Economic Assessment of the Risks and Benefits of Direct Access to INTELSAT in the United States* at 13-15 (“Brattle Analysis”).

<sup>15</sup> *Id.*, *passim*.

<sup>16</sup> Compare *Id.* at pp.66-67 with *Direct Access Order* at ¶95.

Signatory has an incentive to develop their U.S. activities at artificially low prices, that some foreign Signatories indeed have strong incentives to oppose such pricing, and that it is improbable that a majority of Signatories would support uneconomically priced IUCs through an INTELSAT Board of Governor's vote.

The FCC based its theory of potential competitive concerns raised by foreign Signatories with direct access on the following premise: "There may be potential incentives for Signatories to depress IUC rates for direct access to uneconomically low levels, *i.e.*, to levels that do not reflect INTELSAT's full costs of providing direct access in the U.S. market."<sup>17</sup> According to this theory, foreign Signatories who want to purchase direct access from INTELSAT in the U.S. will want to purchase it at low prices. Because foreign Signatories, according to the FCC, have the ability "to influence direct access prices, they may be able to develop their U.S. activities at artificially low prices, which could have an adverse competitive effect on Comsat and other international service providers operating in the U.S."<sup>18</sup>

The FCC argues that because most foreign Signatories are vertically integrated and will purchase INTELSAT services for sale to their own retail customers, they will be relatively indifferent about the level of the IUC because the IUC is "primarily a transfer price."<sup>19</sup> According to the FCC, as long as the "usage shares and ownership shares of

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<sup>17</sup> *Direct Access Order* at ¶96. The type of pricing at "uneconomically low levels" that the FCC discusses in the Report and Order appears to be in the context of fully recovered operating costs and historical investment costs. This Petition analyzes whether, in fact, foreign Signatories have the incentive to price below this level of costs in order "to develop their U.S. activities at artificially low prices." See also Affidavit of John H. Preston, November 8, 1999, at p.7 n.23 and accompanying text ("Preston Aff.").

<sup>18</sup> *Direct Access Order* at ¶96.

<sup>19</sup> *Id.*

INTELSAT are roughly balanced, Signatories who are also retail service providers will be unaffected by low IUC rates and have no incentive to resist lowering IUC rates where to do so is otherwise advantageous.”<sup>20</sup>

The FCC's analysis is defective because no foreign Signatory has an economic incentive to establish artificially low IUC prices in order to develop their U.S. activities, and some foreign Signatories have incentives to strongly oppose such pricing because of the effect of lower IUCs on activities outside the U.S. Limitations on direct access in the U.S. therefore provide no necessary or beneficial competitive safeguard, while imposing a market distortion that does harm U.S. consumers.

**A. Granting Direct Access to Foreign Signatories Will Not Provide an Incentive to Lower the IUC to “Uneconomically Low Levels”**

The FCC asserts that foreign Signatories may have an incentive to lower the IUC to uneconomically low levels. Foreign Signatories would not have any such incentive, principally because: (1) A lower IUC will not give foreign Signatories any competitive advantage in the U.S. market; and (2) in countries where Level 3 direct access is permitted, Signatories would have a strong incentive to oppose artificially low IUCs, which would result in a subsidy from the foreign Signatory to competing Level 3 direct access users in that country.

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<sup>20</sup> *Id.* Notably, the FCC does not consider provisions in the INTELSAT Operating Agreement establishing that IUCs shall cover costs, thereby providing a safeguard against the theoretical Signatory incentives. *See* Operating Agreement Relating to the International Telecommunications Satellite Organization, “INTELSAT,” 23 U.S.T. 4091 (August 20, 1971) (“INTELSAT Operating Agreement”) at Article 8(a) (“Such charges shall have the objective of covering the operating, maintenance and administrative costs of INTELSAT, the provisions of such operating funds as the Board of Governors may determine to be necessary, the amortization of investment made by Signatories in INTELSAT and compensation for use of the capital of Signatories.”).

As shown in the attached affidavit of economist John H. Preston of Economists Incorporated, because the INTELSAT Agreement contains a requirement that an IUC must be offered on a non-discriminatory basis to all users of a given service, a lower IUC cannot give a foreign Signatory operating in the U.S. any competitive advantage over Comsat or any other direct access user in the U.S.<sup>21</sup> Indeed, in the improbable event that Signatories holding a majority of voting shares did vote to reduce the IUC to artificially low levels, <sup>22</sup>/ all carriers and users operating in the U.S. with direct access would be charged the same low rate. Rather than harming other direct access carriers and users operating in the U.S., foreign Signatories would be benefiting their Level 3 competitors both in the U.S. and in their home countries because these competitors will receive exactly the same rate reductions.<sup>23</sup> No rational Signatory would lower its cost of entry into the U.S. market in a manner that would extend the same benefits to its competitors, at a potential cost to itself of a reduced return on its INTELSAT investment

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<sup>21</sup> See Preston Aff at pp. 4, 8-9. The INTELSAT Agreement contains provisions that would prevent discriminatory pricing advantageous to foreign Signatories. Agreement Relating to the International Telecommunications Satellite Organization, "INTELSAT," 23 U.S.T. 3813; TIAS No. 7532, (February 12, 1973) ("INTELSAT Agreement") at Article V(d) ("The rates of space segment utilization charge for each type of utilization shall be the same for all applicants for space segment capacity for that type of utilization."); *Id.* at Article III(a) ("... INTELSAT shall have as its prime objective the provision ... of the space segment required for international public telecommunications services of high quality and reliability to be available on a *non-discriminatory basis to all areas of the world.*") (emphasis added).

<sup>22</sup> BTNA shows in Section III.B, below, that even if some foreign Signatories had an incentive to lower IUCs to artificially low levels, voting arrangements within INTELSAT make carrying out of such a scheme a practical improbability.

<sup>23</sup> See Preston Aff. at p.9 n.29. Comsat would be harmed because it would suffer a reduced distribution of returns at the same time that increased utilization by Level 3 users would require it to increase INTELSAT investment. All other U.S. carriers, however, would benefit by receiving INTELSAT services at below cost prices.

based on utilization in markets outside the U.S. (*i.e.*, in countries where it is a Signatory or Level 4 user). Because there is no incentive to support uneconomic pricing as part of a U.S. market entry strategy, there is no economic rationale for the FCC to restrict direct access to INTELSAT by foreign Signatories on their U.S.-home country routes.

The inability for any Signatory to achieve a competitive advantage in the U.S. through artificially low prices is reason enough for the FCC to remove its restriction. Nonetheless, we demonstrate that some foreign Signatories have additional incentives to oppose below cost IUCs because of their effects in markets outside the U.S.<sup>24</sup> Because IUCs vary neither by country nor user, in any of the 46 member countries where Level 3 direct access is available, artificially low IUCs would result in a Signatory subsidy to competing Level 3 direct access users in the Signatory's home country. As with Comsat in the U.S., such Signatories would receive reduced compensation for their INTELSAT investment while simultaneously being required by INTELSAT to make additional investments in excess of their own utilization based on the utilization of the Level 3 users in their own countries.<sup>25</sup>

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<sup>24</sup> Below-cost IUC pricing could not be contained to the U.S. because, for a given service and duration, INTELSAT charges the same IUC on a worldwide basis. *See Direct Access Order* at ¶¶7-8; INTELSAT Agreement, Article V(d) and Article III(a).

<sup>25</sup> In this regard, the incentives of foreign Signatories will be aligned with the incentives of Comsat. Both will oppose below-cost reductions in the IUC. Furthermore, even Signatories of member countries that have not granted Level 3 or Level 4 direct access will have incentives to oppose lowering IUCs because all Signatories would face a reduction in investment returns from the sale of below cost services to D.A.T.E.s (including Level 3 direct access providers in D.A.T.E. countries). D.A.T.E.s represent non-member countries who utilize INTELSAT services but who do not invest in INTELSAT. *Preston Aff.* at p.14 n.38.

The financial harm to foreign Signatories will be exacerbated to the extent that artificially low prices cause Level 3 users to expand their usage.<sup>26</sup> Specifically, subsidized pricing to Level 3 users will (1) attract new Level 3 direct access competitors; (2) lead existing Level 3 direct access users to expand their purchases of INTELSAT services; and (3) wherever users can select either Level 3 or Level 4 status, create an incentive for existing Level 4 investors to seek Level 3 status to obtain the benefits of artificially low prices without the burden of making less remunerative INTELSAT investments.<sup>27</sup> This activity will take place without the foreign Signatory having created any competitive advantage for itself, and with the additional disadvantage of a reduced rate of return for the Signatory on an increased investment share. Thus in countries where Level 3 direct access is permitted (and also where both Level 3 and Level 4 direct access are permitted), Signatories should have a powerful additional incentive to discourage the INTELSAT Board of Governors from adopting below-cost IUCs.

**B. It Is Improbable that a Majority of Signatories Would Pursue an Unprofitable Strategy through a Board of Governor's Vote**

When the FCC concluded that competitive concerns with foreign Signatories would likely be realized if they did not adopt the subject restriction, they did not analyze the voting strength of INTELSAT members to determine whether it was in any way likely that a majority of Signatory votes would be in favor of lowering IUCs to artificially low levels. Such an analysis would properly take into consideration which INTELSAT members had the incentive to seek below cost IUCs and which did not. BTNA's analysis

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<sup>26</sup> *Id.* at p.10.

<sup>27</sup> *Id.*

in Section A above shows that no foreign Signatory has an economic incentive to institute artificially low IUCs to develop a U.S. presence, and that some Signatories in countries where Level 3 and Level 4 direct access is available would have strong incentives to oppose such pricing due to the potential imbalance in investment share and utilization.<sup>28</sup> By combining that analysis of Signatory economic incentives, with the following analysis of the voting strength of differently situated Signatories, it appears improbable that a Board of Governor's vote would approve uneconomically priced IUCs. <sup>29</sup>

Under current practice, INTELSAT tariff changes are proposed by staff management on a cost recovery basis with reference to Article 8 of the INTELSAT Operating Agreement.<sup>31</sup> All tariff changes are subject to approval by the Board of Governors. At any time a Signatory is theoretically able to submit a position paper to the Board of Governors concerning rate changes, although anecdotal evidence from conversations with INTELSAT suggests that there is no history of a Signatory having done so. If a proposal that has been advanced by staff or a Signatory generates sufficient

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<sup>28</sup> As discussed in note 25, *supra*, in addition to the Signatories in countries with both Level 3 and Level 4 direct access, below cost IUCs may impact Signatories with no in-country competition, due to utilization of INTELSAT services in non-member countries by D.A.T.E.s and direct access users in their countries. No INTELSAT investment is required based on utilization in such non-member countries.

<sup>29</sup> See generally Preston Aff. at pp.5-6, 11-14. Mr. Preston's affidavit includes detailed analysis of the economic significance of Level 3 and Level 4 Direct Access in both Signatory and D.A.T.E. countries. He also analyzes the precision with which an economic assessment of incentives can be made on a country by country basis, and reaches general conclusions about these incentives in accordance with the data that is publicly available.

<sup>30</sup> [Intentionally blank – software formatting error]

<sup>31</sup> See note 20 *supra* discussing INTELSAT Operating Agreement, Article 8.

controversy that a roll call vote is required among the Signatories, then a greater than 50% majority of voting shares is required to carry the proposal.<sup>32</sup>

The voting strength of Signatories in countries granting Level 3 or Level 4 direct access (including Comsat's voting strength) make it improbable that a sufficient number of votes could be obtained to lower IUCs to artificially low levels. Comsat, with an investment share of 19.84%, clearly has a strong incentive to oppose artificially low IUCs. In addition to Comsat, a majority of votes against a proposal to lower IUCs could be gained with another 30.17% of total voting shares.<sup>33</sup>

Mr. Preston's affidavit shows that 81 member countries where Level 3 or Level 4 direct access is permitted (excluding the U.S. and D.A.T.E. countries) account for 55.24% of the investment in INTELSAT.<sup>34</sup> When combined with the 19.84% investment share of Comsat, the 82 countries with Level 3 or Level 4 direct access have an investment share of 75.08%. Although there is insufficient publicly available data to determine the level of non-Signatory usage in each Level 3 and Level 4 country, the distribution of investment shares does suggest that it would be improbable that a sufficient number of votes could be obtained to lower IUCs to artificially low levels. This probability analysis is based on fundamental facts: no Signatory has an incentive to lower IUCs to develop a market position, and Signatories in several countries that

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<sup>32</sup> Under INTELSAT procedures, a Signatory holds the voting rights for investment shares owned by Level 4 users in the Signatory's country.

<sup>33</sup> INTELSAT 1998 Annual Report (showing investment shares by country as of April 12, 1999).

<sup>34</sup> Preston Aff. at p.14.

<sup>35</sup> [Intentionally blank – software formatting error]

account for a significant portion of INTELSAT votes have additional incentives to oppose the lowering of IUCs.

The improbability of a vote in favor of artificially low IUCs can also be demonstrated by examining the investment shares of Signatories who, regardless of the level of direct access competition in their country, have investment shares which exceed their utilization due to a reallocation of shares among investors. INTELSAT most recently readjusted its investment shares on March 1, 1999 based on current utilization rates and investors' desires to have investment shares greater than or less than their utilization shares. As a result of this process, investors whose investment shares exceed their utilization shares hold a significant majority of total INTELSAT investment. For example, the 50 largest investing countries in INTELSAT have an 89.69% share of total INTELSAT investment. Signatories in 28 of the 50 largest investing countries have investment shares greater than their utilization shares. These 28 countries account for 68.08% of total INTELSAT investment. *See* INTELSAT, "March 1, 1999 Determination of Investment Shares." Voting shares of these countries will approximate the investment shares. Signatories in these countries will have a strong incentive to oppose below-cost IUCs because below-cost IUCs would reduce the returns from their investments.

If Signatories vote according to their economic interests as analyzed above, the Board of Governors would reject any proposal to adopt uneconomic IUC pricing. Because the Commission's competitive concerns are not likely to be realized, their prescriptive cure is unnecessary and should be eliminated. 36

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36 *Direct Access Order* at ¶99 ("[I]f our competitive concerns regarding dominant Signatories are not likely to be realized, we will reevaluate this decision.").

#### **IV. RESTRICTING DIRECT ACCESS BY FOREIGN SIGNATORIES IS INCONSISTENT WITH THE PUBLIC INTEREST**

The Commission does not promote or protect competition in the U.S. by restricting participation by foreign Signatories. Instead, the rule limiting availability of direct access on specific routes harms and distorts competition by disabling an entire class of providers from competing on equal terms for the business of retail customers in the U.S. The Commission would better achieve its public interest objectives by allowing open competition, and to address any actual anti-competitive behavior through conditions and enforcement powers over Section 214 authorizations and Title III licenses.

For the foreign Signatories who are potential competitors to established U.S. carriers, the ability to provide high quality services between the U.S. and the Signatory's home country is likely to hold an appealing value to customers. Without direct access, however, a Signatory who may have a superior offering in terms of technical expertise or customer care will be disabled from competing on price. This unnecessary market distortion impairs competition to the detriment of U.S. consumers.

Rather than limiting market participation based on speculation about anti-competitive behavior, however improbable, the Commission should address actual anti-competitive behavior, if it arises, through the existing competitive safeguards and enforcement powers over Section 214 Authorizations and Title III licenses. The Commission already imposes safeguards and restrictions on carriers that are classified as dominant on particular routes: rules that would apply to the majority of Signatories when participating in the U.S. market. Such safeguards provide the Commission with ample opportunity to monitor retail activities, and further ensure transparency of provisioning from foreign affiliates through limited structural separations and the no special

concessions requirements.<sup>37</sup> To the extent that the Commission discovers actual anti-competitive activity by a Signatory, it can consider use of its full enforcement powers over the Signatory's U.S. direct access operations, whether by imposing conditions, fines or revocation of authorizations and licenses.

Analysis in this Petition demonstrates that foreign Signatories do not create competitive concerns to other U.S. direct access users, whether as U.S. market participants or otherwise, and that open market opportunities for such carriers is most consistent with Commission goals and the public interest. <sup>38</sup>

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<sup>37</sup> 47 C.F.R. §63.10(c) requires quarterly reporting of traffic and revenue, provisioning and maintenance details, and circuit status. It also requires limited structural separation, including separate corporate affiliates, separate books of accounts and a prohibition on joint ownership of transmission or switching facilities. *See also* 47 C.F.R. §63.14. In specific terms, the no special concessions rule prohibits a U.S. carrier from agreeing to accept a special concession from any foreign carrier with market power on the foreign end of a U.S. international route.

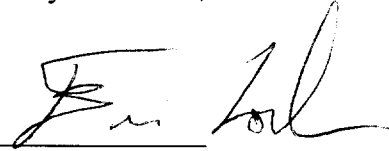
<sup>38</sup> *See Rules and Policies on Foreign Participation in the U.S. Telecommunications Market*, 12 F.C.C. Rcd 23891 (1997) (Order guided by objective of promoting competition in the U.S. market, and of achieving a more competitive global market for all basic telecommunications services).

## V. CONCLUSION

For the foregoing reasons, BTNA respectfully requests that the FCC reconsider and remove the restrictions imposed in the *Direct Access Order* on foreign Signatories and their greater than 50 percent owned affiliates, thereby allowing such parties to purchase direct access in the U.S. for service to or from any specific foreign country in which the Signatory itself uses 50 percent or more of all INTELSAT capacity.

Respectfully submitted,

By: \_\_\_\_\_



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<b>In the Matter of</b>	)	<b>IB Docket No. 98-192</b>
	)	<b>File No. 60-SAT-ISP-97</b>
<b>Direct Access to the</b>	)	
<b>INTELSAT System</b>	)	

**AFFIDAVIT OF JOHN H. PRESTON**

**I. Introduction**

**A. Scope of Affidavit**

My name is John Preston. In support of its Petition for Reconsideration, BT North America, Inc. ("BTNA") has asked me to provide an economic analysis in response to the Federal Communications Commission's ("FCC's") recent decision denying direct access by foreign Signatories to INTELSAT on their U.S.-home country routes.<sup>1</sup> While the FCC granted direct access by most users in the U.S. to INTELSAT, the agency denied access in the U.S. to foreign Signatories on routes between the U.S. and a foreign country where a foreign Signatory had greater than a 50% share of INTELSAT capacity utilized in that country.<sup>2</sup> As a practical matter, this 50% threshold would result in a denial of

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<sup>1</sup> See FCC Report and Order *In the Matter of Direct Access to the INTELSAT System* (IB Docket No: 98-192), released September 16, 1999 (hereafter "*Direct Access Order*"). Direct access by foreign Signatories is covered primarily in ¶¶95-100 of the *Direct Access Order*.

<sup>2</sup> *Direct Access Order*, ¶98.

direct access in the U.S. to virtually all foreign Signatories on their U.S.-home country routes.

## **B. Summary of Argument**

In this Affidavit, I reach three main conclusions:

- In contrast to the findings in the *Direct Access Order*, I conclude that foreign Signatories have no economic incentive to lower the charge for access to the INTELSAT space system in order to begin competing in the U.S. “at artificially low prices.”<sup>3</sup> This conclusion is, in and of itself, sufficient to demonstrate that denial of direct access to foreign Signatories on U.S.-home country routes serves no pro-competitive purpose. Instead, it harms competition because it prevents an entire class of providers (foreign Signatories) from effectively competing for the business of retail customers in the U.S. seeking to use INTELSAT services.
- Some foreign Signatories, which appear to account for a significant portion of INTELSAT votes, would incur a financial loss if the access charge were reduced to “uneconomically low levels.”<sup>4</sup> These foreign Signatories would have additional incentives to oppose the lowering of access charges.
- An analysis of voting rights in INTELSAT shows that it is improbable that Signatories comprising a majority of INTELSAT ownership would vote to lower IUCs to artificially low levels.

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3      *Direct Access Order*, ¶96.

4      *Id.*

## **C. Qualifications**

I have been a professional economist since 1975. I was employed as an economist at the Antitrust Division of the Department of Justice for 10 years and, since 1985, I have been employed at Economists Incorporated, a firm that specializes in antitrust and regulatory analysis. I am currently a Vice President of Economists Incorporated. While at Economists Incorporated, I have provided economic analyses on a number of telecommunications matters including the following: the BT/AT&T Global Venture, BT/MCI I, BT/MCI II, the Qwest/U S WEST merger, the acquisition of ConTel (including its satellite business) by GTE, and the sale of the GTE satellite business to GE Americom. I received my graduate training in economics at the University of Michigan. A copy of my curriculum vitae is attached as Exhibit A.

## **II. Background**

### **A. INTELSAT Utilization Charges**

A long-term objective of INTELSAT is to generate revenues from the provision of its services to cover the cost of operations and the cost of capital. The Board of Governors sets the target rate of return on invested capital. Each Signatory is entitled to receive the same target rate of return.<sup>5</sup>

In order to generate revenues to cover the costs of operating its satellite system, INTELSAT charges an INTELSAT utilization charge ("IUC") to users of the system. The IUC varies by type of service and duration of lease.<sup>6</sup> The IUCs charged by INTELSAT

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<sup>5</sup> *Direct Access Order*, ¶6. See also the INTELSAT Operating Agreement, Article 8 (a). "[INTELSAT space segment utilization charges] shall have the objective of covering the operating, maintenance and administrative costs of INTELSAT, the provisions of such operating funds as the Board of Governors may determine to be necessary, the amortization of investment made by Signatories in INTELSAT and compensation for use of the capital of Signatories."

<sup>6</sup> In addition to duration of lease, factors used to determine an IUC include beam coverage, spectrum capacity, and data rate. IUCs are listed in the INTELSAT Tariff Manual. *Direct Access Order*, ¶7.

do not vary by user, country of origin, or country of destination. That is, INTELSAT offers its services on a non-discriminatory basis.<sup>7</sup>

## **B. Direct Access to INTELSAT**

Beginning in 1994, INTELSAT began to permit direct access to INTELSAT but only in countries where the Signatory authorized direct access. Of particular relevance to this matter are Level 3 direct access and Level 4 direct access.<sup>8</sup> “Level 3 direct access permits customers to enter into a contractual agreement with INTELSAT for ordering, receiving, and paying for INTELSAT space segment capacity at the same rates that INTELSAT charges its Signatories.”<sup>9</sup> A Signatory is required to make investments in INTELSAT in proportion not only to its own utilization of the INTELSAT system, but also in proportion to the utilization of the INTELSAT system by Level 3 customers in the Signatory’s own country.<sup>10</sup> Level 4 direct access also permits a user to gain access at the same rates that INTELSAT charges Signatories. In addition, Level 4 direct access requires a user to make investments in INTELSAT in proportion to its usage of the INTELSAT system.<sup>11</sup>

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7 Article III (a) of the INTELSAT Agreement specifies that “[INTELSAT’s] prime objective [shall be] the provision, on a commercial basis, of the space segment required for international public telecommunications services of high quality and reliability to be available on a non-discriminatory basis to all areas of the world.”

8 There are two additional levels of direct access. Level 1 direct access provides a user access to INTELSAT operational and technical matters. Level 2 direct access provides a user access to INTELSAT tariffs and service terms and conditions. Source: “Report by the Board of Governors on INTELSAT Access Arrangements,” March 18, 1997.

9 *Direct Access Order*, ¶8. (Emphasis added.) See also the INTELSAT Agreement, Article V (d). “All users of the INTELSAT space segment shall pay utilization charges determined in accordance with the provisions of this Agreement and the Operating Agreement. The rates of space segment utilization charge for each type of utilization shall be the same for all applicants for space segment capacity for that type of utilization.”

10 *Direct Access Order*, ¶9. “Furthermore, a Signatory permitting Level 3 direct access will earn a return on its investment in space segment capacity used by the Level 3 customer (currently between 14 and 18 percent).”

11 *Direct Access Order*, ¶8. However, a Level 4 user generally does not have the right to participate in governance matters.

In its *Direct Access Order*, the FCC granted only Level 3 direct access. It did not grant Level 4 direct access.

### **C. The Economic Significance of Level 3 Direct Access and Level 4 Direct Access**

There are currently 143 member countries participating in INTELSAT. In addition, there are 46 non-member countries, known as Duly Authorized Telecommunication Entities ("D.A.T.E.s"), that utilize INTELSAT services.<sup>12</sup>

The most recent compilation by INTELSAT shows that there are now 100 countries where Level 3 or Level 4 direct access is allowed.<sup>13</sup> Of these 100 countries, Level 3 direct access is allowed in 65 countries and Level 4 direct access is allowed in 35 countries.<sup>14</sup> Of the 65 countries where Level 3 direct access is allowed, 46 are member countries and 19 are non-member countries (or D.A.T.E.s). This INTELSAT compilation reflects Level 3 or Level 4 direct access privileges that have been granted to at least one user in each of the 100 countries. INTELSAT does not state whether companies that have been granted Level 3 or Level 4 direct access privileges have actually taken up such privileges. According to INTELSAT, the number of direct access users of INTELSAT, increased from 350 in 1997 to 480 currently.<sup>15</sup> These totals include Level 1 through Level 4 users.<sup>16</sup>

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12 Information provided by INTELSAT.

13 INTELSAT compilation, September 24, 1999. Most Signatories and D.A.T.E.s grant the level of direct access on a case-by-case basis. They may grant access privileges at one or more levels (Levels 1 to 4). Several countries, including the UK, China, Finland, France, and Austria, grant "blanket authorization," which enables the user to gain access directly from INTELSAT without first seeking authorization from its Signatory. Information provided by INTELSAT and *Direct Access Order*, ¶9.

14 INTELSAT compilation, September 24, 1999.

15 Information provided by INTELSAT, including INTELSAT 1997 Annual Report.

16 While INTELSAT does identify the number of Level 4 investors (there are 59), INTELSAT does not provide a numerical breakdown between the number of Level 1, Level 2, and Level 3 users.

Level 3 and Level 4 direct access customers now account for about 20% of INTELSAT's total revenues.<sup>17</sup> Signatories and D.A.T.E.s account for the remaining 80%. The Level 3 and Level 4 direct access users' share of INTELSAT revenues grew from 17.4% in 1997 to 20% in 1998,<sup>18</sup> but most of this increase appears to have come from increased utilization by Level 3 direct access users. In 1997, the investment share of Level 4 direct access investors was 6.5%, which grew to 6.6% in 1998.<sup>19</sup> This implies that the utilization share of Level 3 direct access users increased from approximately 10.9% in 1997 to approximately 13.4% in 1998, an increase of 23.0%. In contrast, overall INTELSAT revenues from the provision of telecommunications services grew by only 6.1% between 1997 and 1998.<sup>20</sup>

The FCC noted that due to direct access, foreign carriers "have realized greater cost savings, efficiencies, and service benefits by directly accessing INTELSAT rather than going solely through a Signatory."<sup>21</sup> The FCC adopted Level 3 direct access to enable U.S. carriers to compete more effectively with foreign carriers. "The availability of additional choices are increasingly important to U.S. carriers and users because they must compete on a global basis with their foreign counterparts who presently can obtain direct access, a choice available in 94 countries . . . The competitive nature of the global telecommunications market requires that we assure U.S. carriers and service providers the availability of choices that their foreign competitors now enjoy."<sup>22</sup>

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17 According the INTELSAT 1998 Annual Report, p. 7, direct access users accounted for 20% of total revenues of INTELSAT. Presumably, revenues from the provision of Level 1 and Level 2 direct access services were negligible.

18 INTELSAT 1998 Annual Report, p. 7. Revenues from direct access users grew by 15% between 1997 and 1998 according to INTELSAT.

19 INTELSAT 1997 Annual Report and INTELSAT 1998 Annual Report. In the past few years, some Level 4 investors have sought and received reductions in their investment shares in INTELSAT. The utilization share of Level 4 investors in the aggregate would, thus, be somewhat larger than their investment share.

20 INTELSAT 1998 Annual Report, p. 25. INTELSAT revenues from the provision of telecommunications services were \$961.6 million in 1997 and \$1,020.4 million in 1998.

21 *Direct Access Order*, ¶20.

22 *Direct Access Order*, ¶20.

### **III. Economic Analysis of the FCC Theory that Foreign Signatories Will Have an Incentive to Lower IUCs to “uneconomically low levels”**

#### **A. The FCC Theory of Potential Competitive Concerns Raised by Direct Access by Foreign Signatories**

The FCC theory of potential competitive concerns raised by direct access by foreign Signatories is based on the following premise: “There may be potential incentives for Signatories to depress IUC rates for direct access to uneconomically low levels, *i.e.* to levels that do not reflect INTELSAT’s full costs of providing direct access in the U.S. market.”<sup>23</sup> According to the FCC theory, foreign Signatories who want to purchase direct access from INTELSAT in the U.S. will want to purchase it at low prices. Since foreign Signatories have the ability “to influence direct access prices, they may be able to develop their U.S. activities at artificially low prices, which could have an adverse competitive impact on Comsat and other international service providers operating in the U.S.”<sup>24</sup> The FCC argues that since most foreign Signatories purchase INTELSAT services for sale to their own retail customers, they will be relatively indifferent about the level of IUC rates because to foreign Signatories the IUC rates are “primarily a transfer price.”<sup>25</sup> According to the FCC, as long as the “usage shares and ownership shares of INTELSAT are roughly balanced, Signatories who are also retail service providers will be unaffected by low IUC rates and have no incentive to resist lowering IUC rates where to do so is otherwise advantageous.”<sup>26</sup>

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23     *Direct Access Order*, ¶96. The type of pricing at “uneconomically low levels” that the FCC discusses in the *Direct Access Order* appears to be in the context of fully recovered operating costs and historical investment costs. My Affidavit analyzes whether, in fact, foreign Signatories have the incentive to price below this level of costs in order “to develop their U.S. activities at artificially low prices.”

24     Id.

25     Id.

26     Id.

**B. Granting Direct Access to Foreign Signatories Will Not Provide An Incentive to Lower IUCs to “Uneconomically Low Levels”**

**1. Introduction**

The FCC argues that foreign Signatories may have an incentive to lower IUCs to “uneconomically low levels.” This argument fails for two principal reasons: (1) A lower IUC will not give foreign Signatories any competitive advantage in the U.S. market; and (2) In countries where Level 3 direct access is permitted, artificially low IUCs would likely result in a subsidy from the foreign Signatory to competing Level 3 direct access users in that country. The foreign Signatories in Level 3 direct access countries will have a strong incentive to oppose below-cost IUCs in order to avoid subsidizing their Level 3 direct access competitors.

**2. There Is No Incentive for Foreign Signatories to Lower ICUs to “Uneconomically Low Levels”**

The FCC supposes that foreign Signatories “may be able to develop their U.S. activities at artificially low prices, which could have an adverse competitive impact on Comsat and other international service providers operating in the United States.”<sup>27</sup> But the FCC does not explain why foreign Signatories would want to develop their U.S. activities at “artificially low prices,” or how such prices would be advantageous to foreign Signatories.

As the FCC recognized in its *Direct Access Order*, INTELSAT charges the same IUC to all users of a given service, whether the user is a Signatory, a D.A.T.E., a Level 3 user, or a Level 4 user.<sup>28</sup> If foreign Signatories were able to reduce IUCs to artificially

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<sup>27</sup> Id. Level 3 and Level 4 direct access is now available in 100 countries, including most European countries. (See Section II. C., above.) The countries in which Level 3 or Level 4 direct access is available comprise a larger share of INTELSAT business than does the U.S. If lowering IUCs to develop their activities in other countries at artificially low prices were a profitable strategy for foreign Signatories, we would expect that IUCs already would have been reduced. The fact that they have not already been reduced to artificially low levels is evidence that foreign Signatories do not have an incentive to make such reductions.

<sup>28</sup> *Direct Access Order*, ¶8.

low levels, all carriers and users operating in the U.S. would be charged the same rate for each service. That is, Level 3 direct access carriers in the U.S. such as AT&T, MCI WorldCom, and Sprint would be able to enjoy the same low IUC for each service as would foreign Signatories or any other user of INTELSAT services in the U.S. Because foreign Signatories would gain no competitive advantage in the U.S. from low IUCs, they would have no incentive to set artificially low IUCs.<sup>29</sup>

Since there is no incentive for foreign Signatories to develop their U.S. activities at “artificially low prices,” there is no economic rationale for the FCC’s denial of direct access to INTELSAT by foreign Signatories on their U.S.-home country routes. That is a sufficient justification for the removal of the FCC’s restriction on direct access by foreign Signatories. While the denial of direct access to foreign Signatories serves no pro-competitive purpose, it does have anti-competitive effects. Consumers in the U.S. are denied the benefits from competition by an entire class of providers on their U.S.-home country routes.

### **3. Some Foreign Signatories Will Have Additional Incentives to Oppose Lowering IUCs to Artificially Low Levels**

As was argued immediately above, no foreign Signatory will have an incentive to lower IUCs to artificially low levels. In addition, some foreign Signatories will have additional incentives to oppose artificially low IUCs. The effects of artificially low IUCs could not be confined to the U.S. since, for a given service and duration, INTELSAT charges the same IUC on a worldwide basis to all users.<sup>30</sup> As a consequence, Level 3 providers in countries where Level 3 direct access is permitted would enjoy below-cost access at the expense of their home country Signatories. Since a Signatory is required to

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29 Even if foreign Signatories were able to set artificially low prices, which they have no incentive to do, it is clear that international service providers operating in the U.S. would not be harmed, as claimed by the FCC in ¶96 of the *Direct Access Order*. To the contrary, U.S. international service providers such as AT&T, MCI WorldCom, and Sprint would benefit since they would receive INTELSAT services at below cost prices. Comsat, however, would be harmed since the below cost prices enjoyed by U.S. international carriers would come at the expense of Comsat. As the U.S. Signatory, Comsat would be required to invest in INTELSAT in proportion to the utilization of INTELSAT by Level 3 customers in the U.S. A reduction in IUCs to artificially low levels would reduce the returns on that investment received by Comsat.

30 See INTELSAT Agreement, Article V (d) and Article III (a).

invest in INTELSAT in proportion to the utilization of INTELSAT capacity by Level 3 users in its country, the Signatory's INTELSAT investment will be higher as a result of the existence of Level 3 direct access in the Signatory's country, thereby increasing the Signatory's capacity ownership share relative to its utilization share. As a consequence, reducing IUC rates will reduce the return on the investment it is required to make on behalf of Level 3 users.<sup>31</sup> To further exacerbate the potential financial loss to foreign Signatories, existing Level 3 users would likely seek to expand their purchases of INTELSAT services and new customers would likely seek Level 3 status. Existing Level 4 users would also have an incentive to seek Level 3 status, where permitted, to take advantage of the artificially low prices. To the extent Level 3 usage was expanded due to artificially low prices, the Signatory would have to increase its required investment to accommodate the increase in Level 3 usage, thereby increasing the Signatory's financial loss.<sup>32</sup>

In countries where Level 3 and Level 4 direct access is permitted, Signatories, including Comsat, would likely have a powerful incentive to oppose lowering IUCs to artificially low levels.<sup>33</sup> If they were to support such pricing, they would be subsidizing their Level 3 competitors and lowering the returns from their investment.<sup>34</sup>

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31 The Signatory will also receive a reduced return on the investment made in relation to its own usage of INTELSAT capacity to the extent its investment share exceeds its utilization share. Signatories and Level 4 direct access customers commit to take an investment share in line with utilization. INTELSAT investment shareholders can seek higher or lower shares than the utilization-driven shareholding at investment share redeterminations. There is no guarantee that requests for increases/decreases will be satisfied.

32 It could be argued that in countries where Level 3 or Level 4 direct access is now permitted, the Signatories could decide to sharply limit or even eliminate direct access, thereby removing or sharply reducing the disincentive to vote for lower IUCs. Such action, however, would be directly contrary to the liberalization in telecommunications markets that is occurring in countries and regions throughout the world. Moreover, as discussed above, there is no incentive for Signatories to take such actions.

33 Thus, the incentives of foreign Signatories will be aligned with the incentives of Comsat in the U.S. Since Comsat and foreign Signatories in countries with Level 3 access would suffer investment losses with reductions in the IUC to artificially low levels with no counterbalancing benefits, they will strongly oppose such reductions.

34 Furthermore, the avoidance of below-cost IUCs is reflected in one of the governing principles of INTELSAT. Article 8 (a) of the INTELSAT Operating Agreement requires that the IUC prices be set at a level that recovers its operating and capital costs.

#### **IV. Investment Shares in INTELSAT and Implications for the Likelihood that INTELSAT Members Would Vote to Reduce IUCs to Artificially Low Levels**

##### **A. Introduction**

The FCC did not analyze the voting strength of INTELSAT members to determine whether it was at all likely that a majority of votes would be in favor of lowering IUCs to artificially low levels. Such an analysis would properly take into consideration which members had the incentive to seek low IUCs and which members did not. This section examines the voting strength of Signatories in countries granting Level 3 or Level 4 direct access in combination with Comsat's voting strength.

It is difficult to determine with precision the amount of Level 3 direct access and Level 4 direct access within individual countries. While INTELSAT does make some information available concerning the Level 3 and Level 4 direct access (see Section II. C., above), it does not provide enough information to make a full economic assessment on a country by country basis of the incentives created by Level 3 and Level 4 direct access to oppose reductions in IUCs to artificially low levels. Nonetheless, enough information on Level 3 and Level 4 direct access is provided by INTELSAT to reach some general conclusions regarding these incentives.

As discussed in Section II.C. above, Level 3 direct access customers account for approximately 13.4% of total INTELSAT telecommunications revenues. Revenues from Level 3 direct access customers appear to have grown between 1997 and 1998 at a much faster rate than total INTELSAT telecommunications revenues. The magnitude of this percentage (approximately 13.4%) indicates that many of the 46 member countries granting direct access privileges have significant and active Level 3 direct access customers. In addition, this percentage would also reflect Level 3 direct access activity in countries that permit both Level 3 and Level 4 direct access.

The growing economic significance of Level 3 direct access customers within INTELSAT is also reflected in the *Direct Access Order*, which, in part, based its decision to grant Level 3 direct access in the U.S. on the amount of Level 3 direct access activity in other countries. The FCC noted that due to direct access, foreign carriers "have

realized greater cost savings, efficiencies, and service benefits by directly accessing INTELSAT rather than going solely through a Signatory.”<sup>35</sup> “The availability of additional choices are increasingly important to U.S. carriers and users because they must compete on a global basis with their foreign counterparts who presently can obtain direct access, a choice available in 94 countries . . . The competitive nature of the global telecommunications market requires that we assure U.S. carriers and service providers the availability of choices that their foreign competitors now enjoy.”<sup>36</sup>

**B. The Voting Strength of Countries Granting Level 3 or Level 4 Direct Access in Combination with Comsat’s Voting Strength**

Based on the analysis in Section III B. above, no foreign Signatory will have an incentive to seek lower IUCs. Furthermore, Signatories in countries granting Level 3 or Level 4 direct access may have additional incentives to oppose lowering IUCs to artificially low levels. While this analysis focuses on incentives created by Level 3 and Level 4 direct access, it should be noted that Signatories in some countries have investment shares which exceed their utilization shares due to the reallocation of investment shares from Level 4 investors. Signatories in these countries will have an incentive to oppose below-cost IUCs as a result of these purchases.<sup>37</sup>

Comsat clearly has a strong incentive to oppose below-cost IUC rates because it would suffer a significant financial loss if below-cost IUCs were implemented. Comsat’s investment share in INTELSAT as of April 12, 1999 was 19.84%. A straight majority of votes against lowering IUC rates would therefore require an additional 30.17% of total voting shares.

Table 1 below reflects the investment shares by the direct access status of all INTELSAT member countries. The sources of the information in Table 1 are (1) the section in the INTELSAT 1998 Annual Report showing investment shares by investor

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35 *Direct Access Order*, ¶20.

36 *Direct Access Order*, ¶20.

37 Investment shares given up by Level 4 investors have been reallocated to Signatories desiring to increase their investment shares, thereby increasing the investment shares of those Signatories relative to their utilization shares.

<b>Table 1: INTELSAT Investment Shares by Country Grouped by Direct Access Status</b>		
	<b>Investment Share in INTELSAT</b>	<b>Number of Countries</b>
Countries Granting Up to Level 3 Direct Access	24.07%	46
Countries Granting Up to Level 4 Direct Access	31.17%	35
Subtotal Countries Granting Up to Level 3 Direct Access or Level 4 Direct Access	55.24%	81
Comsat	19.84%	1
Subtotal Comsat Plus Countries Granting Up to Level 3 or Level 4 Direct Access	75.08%	82
All Countries Currently Not Granting Up to Level 3 or Level 4 Direct Access (Not Including Comsat)	24.92%	61
Total All INTELSAT Member Countries	100.00%	143
Sources: INTELSAT Annual Report 1998 showing investment shares by country as of 4/12/99 and INTELSAT compilation of countries permitting Level 3 and Level 4 direct access, 9/24/99.		

and country (attached as Exhibit B) and (2) the identification by INTELSAT of countries where Level 3 and Level 4 direct access are permitted (attached as Exhibit C). The investment share for each country includes the investment by the Signatory and by Level 4 access providers, if any. The Signatory for each country ordinarily votes the entire investment share of that country in INTELSAT governing matters. As mentioned in Section II. C. above, Level 4 access providers accounted for 6.6% of total INTELSAT investment in 1998.

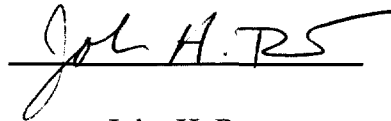
Table 1 shows that in 81 member countries (other than the U.S.), Level 3 or Level 4 direct access is permitted. These countries account for 55.24% of the investment in INTELSAT. When added to the investment share of Comsat (19.84%), the 82 countries with Level 3 or Level 4 direct access have an investment share of 75.08%. While not all Level 3 and Level 4 countries may have active direct access activity, this suggests, nonetheless, that it would be improbable that a sufficient number of votes could be obtained to lower IUCs to artificially low levels. In the first place, no foreign Signatory has an incentive to seek below-cost IUCs. Second, some countries, which appear to account for a significant portion of INTELSAT votes, will have additional incentives to oppose below-cost IUCs.<sup>38</sup>

## **VI. Conclusion**

Based on the analysis and facts presented in this Affidavit, it is highly improbable that INTELSAT members would vote to lower IUCs to artificially low levels. Foreign Signatories would receive no benefit in the U.S. or elsewhere from low IUCs and, thus, would have no incentive to vote for low IUCs. Moreover, the Signatories in some INTELSAT investing countries have strong incentives to oppose such an action. Denying direct access in the U.S. to foreign Signatories on their home routes serves no pro-competitive purpose. The restriction would prevent an entire class of competitors (*i.e.*, foreign Signatories) from effectively competing on their U.S.-home country routes. The likely effect of such action is that competition and consumers in the U.S. will be harmed.

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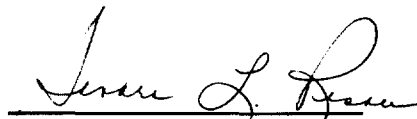
<sup>38</sup> Signatories of member countries that have not granted Level 3 or Level 4 direct access will also have an incentive to oppose lowering IUCs because they, along with all other Signatories, would face a reduction in investment returns from the sale of INTELSAT services to D.A.T.E.s including Level 3 direct access providers in D.A.T.E. countries. D.A.T.E.s are non-member countries who utilize INTELSAT services but who do not invest in INTELSAT.



John H. Preston

DISTRICT OF COLUMBIA )

Subscribed to and sworn before me by said witness, John H. Preston, on this the 8th day of November, A.D., 1999.



Notary Public in and for the  
District of Columbia

**SANDRA L. RESAU**  
**A Notary Public of District of Columbia**  
**My Commission Expires May 31, 2004**